National Life Group®

Legacy IRA Strategy

HELP YOUR CLIENTS MAXIMIZE THEIR LEGACY

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Leverage **IRA Savings**

Individual Retirement Accounts (IRAs) and qualified plans are powerful tools for individuals to accumulate assets for retirement needs and help build a legacy.

In December of 2019, the SECURE Act upended the rules for inherited IRAs, putting an end to the "Stretch IRA" era for most beneficiaries. Under previous tax law, non-spouse beneficiaries could take required minimum distributions based on their life expectancy; the law now requires most non-spousal beneficiaries (not including minor children of the owner, chronically ill or disabled, those less than 10 years younger, and properly drafted "see-through" trusts) to deplete the entire IRA within 10 years. This change may result in additional, higher, and expedited tax burdens for beneficiaries, and ultimately reduce the legacy left.

With this legislative change in effect, there is now an opportunity to use new strategies to help clients who find themselves on either side of this equation.

For IRA and qualified account owners who are not relying on those assets for retirement income, using distributions from the account to fund a permanent life insurance policy can help them convert their account into a potentially larger, tax-free[1] inheritance for their heirs.

With this strategy, the client's IRA account is spent down over a period of several years and the after-tax distributions are used to fund a permanent life insurance policy. This technique requires some current tax-bracket planning to ensure the client's distributions from the IRA aren't causing bracket creep or other tax issues. You'll also want to be aware of estate tax considerations for larger policies that might push the client's estate beyond the exemption limit.

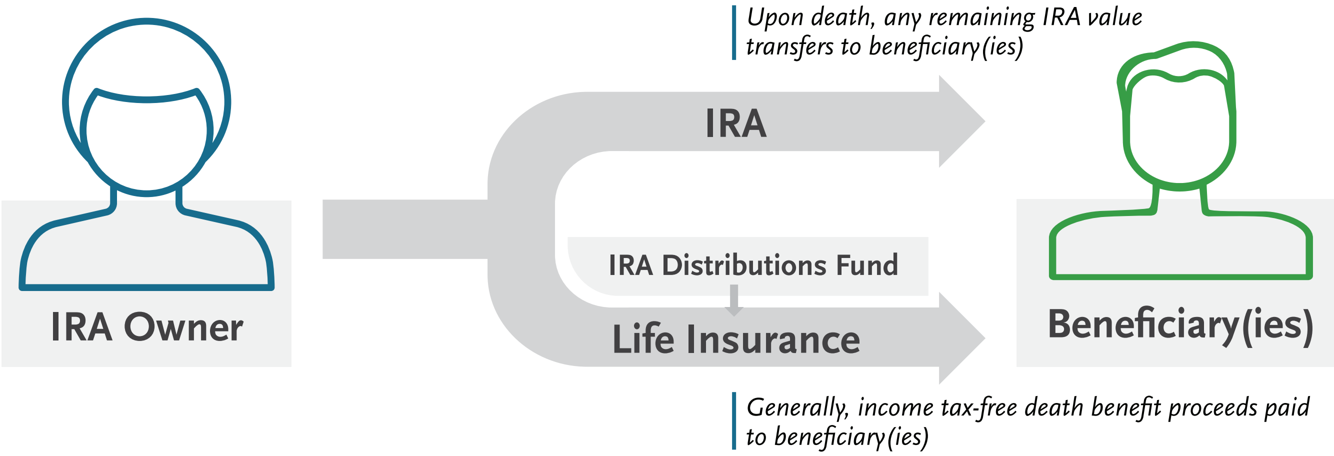
This strategy works well for anyone ranging from the ages of approximately 50 to 70, who is in good health, and has qualified money they don't need in retirement.*

If you have a client who wants to optimize IRA assets beyond their own retirement and leave a lasting legacy, there has never been a better time to leverage the power of life insurance.

* Distributions prior to age 59 ½ may be subject to penalty unless and exception applies.

Legacy IRA Strategy **Using Life Insurance**

In the following scenario, the client uses distributions from their IRA or retirement account to fund a permanent life insurance policy to provide a tax-free legacy to their beneficiaries. Using IRA distributions to purchase a permanent life policy can help your clients' insurance assets work even harder for them and their beneficiaries.



What Could This Mean For Your Clients and Their Beneficiaries?

Let's look at a case study[2] comparing the results of doing nothing versus taking distributions from an IRA to purchase life insurance.

Scenario 1

Jane, age 60, currently has an IRA valued at $1 million that she wishes to leave as a legacy for her son, Joe, currently 30.

No Change — Do Nothing[3]

Jane passes away at age 80. Assuming her IRA earns 4% annually and she saves her RMD distributions in an investment account earning 3% annually, the total value of her accounts would be about $2.1 million at the time of her death.

Joe inherits both accounts and liquidates the IRA as required by the IRS, taking 10 annual distributions and saves the after-tax amount in an investment account earning 3% after-tax. At the end of those 10 years, at his age 60, the total value of his inheritance would be about $2.4 million.

Inherit IRA & Investment Account, take distributions and invest them: **$2,390,924**

Purchase Life Insurance

Jane exhausts her IRA by taking 10 years of annual distributions and purchases a $1.5 million life insurance policy with the after-tax IRA distributions.[4] When Jane passes away at age 80 the policy death benefit is about $3.1 million.

Joe saves the $3.1 million of tax-free life insurance proceeds in an investment account earning 3% annually, after-tax. After 10 years, at his age 60, the value of that account would be about $4.1 million.

Lifetime IRA distributions fund a life insurance policy; Joe invests the policy death benefi: **$4,107,461**

$1,716,537 Difference

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Let's look at the same case study but make a slight addition to the facts.

Scenario 2

Jane, age 60, and her husband Jack, age 65, both have IRA accounts valued at $1 million. They also have a very sizable estate that will be subject to estate taxes once both have passed away. They would like to pass as much of the estate along to Joe as possible without having to worry about its reduction to cover estate tax liability. After consultation with their legal and tax advisors, they have been advised that large qualified plan accounts are the least tax-efficient assets in one's estate due to the possibility of double taxation (potentially subject to both estate and income taxation). Moreover, it has been estimated that the estate tax liability will be roughly $1.5 million once both of them have passed away.

The Strategy

Following the advice of their attorney, Jane and Jack set up an Irrevocable Life Insurance Trust and take out a survivorship policy on both of their lives with a $1.5 million death benefit with the trust being the owner and the beneficiary.[5] Jane and Jack take distributions from their respective IRA accounts and make gifts to the trust over ten years to make the premium payments on the policy.

The Outcome

Jack passes away at age 80, and incurs no estate tax liability upon his death due to the unlimited marital estate tax deduction. Although no death benefit is paid to the trust, the trustee can leverage the policy's cash value to lend money to or purchase assets from Jack's estate to pay any final expenses associated with Jack's death. If done correctly, these transactions may provide liquidity to Jack's estate without resulting in estate inclusion for Jack.

Jane dies 5 years later, also at the age of 80. Following Jane's death, the $3.6 million death benefit from the policy is paid generally income tax-free to the trust. The trust then uses these funds to provide liquidity to Jane's estate to cover any federal and/or state estate taxes and any other final expenses associated with Jane's death (assuming this is done via the trustee lending money to or purchasing assets from Jane's estate). This strategy allows Jack and Jane's estate to be passed along to Joe in the most estate-tax efficient manner, resulting in no reductions in the value of the estate for estate taxes (which were paid via the liquidity provided by the life insurance death proceeds).

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1 Internal Revenue Code § 101(a)(1). There are some exceptions to this rule.

2 Side account is a hypothetical example for illustrative purposes only. Does not represent the actual results of any particular investment or insurance product.

3 Do Nothing" Scenario assumes IRA distributions are taxed at 25%. Jane saves her after-tax RMDs in to a taxable side account earning 3% annually after-tax. The value of that account at Jane's death is $399,090. Jane's $1 m IRA earns 4% annually growing to $1,749,531 at her Death. Joe takes 10 annual pre-tax distributions of $215,701 from the IRA, saving $161,776 to a side account earning 3% after-tax annually for 10 years. The value of this account at that time is $1,854,581. The value of Joe's inherited taxable account after 10 years assuming a 3% after-tax return is $536,343 for a total value of $2,390,924.

4 Life insurance scenario assumes Jane purchases a SummitLife policy-F60, preferred non-tobacco, $1,500,000FV, Option B (Increasing) premium of $92,468/year for 10 years from after-tax distribution from IRA ($123,290 pre-tax). IRA value is $0 at the end of the 10 year distribution period. Policy death benefit at age 80 is $3,056,337. Joe saves this into a side account earning 3% after-tax annually. At the end of 10 years the value of that account is projected to be $4,107,461.

5 This modified scenario assumes the ILIT purchases a Survivorship Indexed Universal Life policy, M65 and F60, preferred nontobacco, $1,500,000FV, Option B (Increasing), $92,468/year for 10 years from after-tax distribution from IRA ($123,920 pre-tax). IRA value is $0 at the end of the 10 year distribution period. Policy death benefit at Jane's death is $3,616,672.